Exhibit E

WESTERN ASSET

Update on the Subprime Mortgage Market

Executive Summary

The turmoil surrounding the U.S. subprime market continues to make headlines worldwide, as subprime mortgage delinquency and default rates steadily rise. News of hedge fund liquidations, rating agency downgrades, and press about the ABX (the index referencing subprime mortgage securities) hitting new lows have caused investors to question the integrity of the subprime market and helped fuel concerns that subprime woes will spill over into the broader market. Given Western Asset's concerns about both the housing market and aggressive mortgage lending practices in the newer vintage subprime originations, we have sought to minimize mortgage credit risk by investing in the highest rated bonds, primarily government agency (GNMA, FNMA, and FHLMC) and AAA rated non-agency securities. In this article, we shed some light on recent events – where market concerns are legitimate and where they are potentially overblown.

- As the subprime market has grown substantially over the last several years, lax underwriting standards and rising home prices have allowed many borrowers to purchase homes that they can not afford.
- The recent tightening of these standards, falling home prices and rising interest rates have contributed to the poor performance of newer vintage subprime loans.
- While recent rating actions as well as price declines of lower rated bonds backed by subprime mortgages and the ABX index have made headlines recently, these issues relate primarily to subprime bonds rated BBB and lower, which make up a relatively small part of the subprime bond market.
- Even using loss assumptions much higher than market expectations, AAA rated subprime bonds are very well protected.
- Market commentary referencing performance problems on higher rated bonds generally refers to bonds issued off ABS collateralized debt obligations (CDOs). Given that ABS CDOs are backed mostly by BBB and lower rated subprime bonds, AAAs in this space are likely to experience distress as they are highly levered to potential losses on subprime collateral.
- Western Asset has invested primarily in AAA rated subprime bonds and did not own any bonds that were watch listed or downgraded by the rating agencies last week. Western Asset has also avoided buying ABS CDOs, even at the AAA level.
- Western Asset will continue to closely monitor developments in housing markets, the economy, and the subprime lending markets, and will look to add exposure to the extent we believe we are being adequately compensated for the risks.

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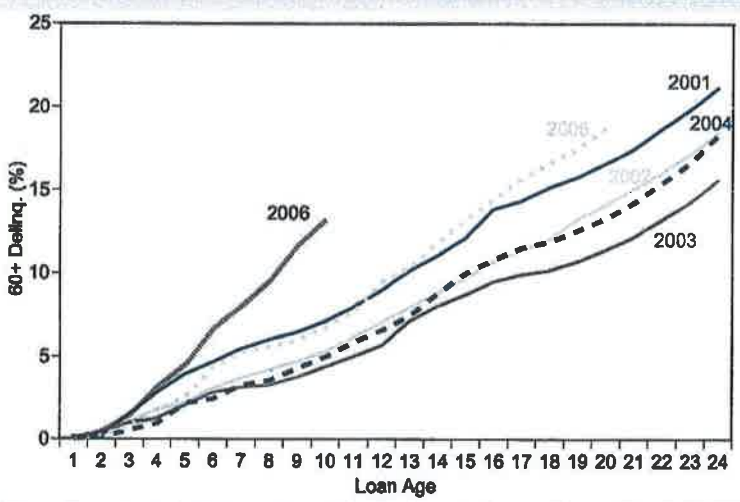
Subprime Market Overview[1]

The subprime market enjoyed unprecedented growth over the five-year period from 2001 to 2006 with annual subprime origination volume more than tripling from $160 billion to $600 billion.[2] Stable interest rates, an improving economy, and rapid home price appreciation over this five-year period led to a benign credit environment for subprime borrowers. Low levels of credit losses on subprime mortgages combined with wide yield spreads relative to other fixed income sectors led to increased investor appetite for securitized subprime mortgages. This increased investor demand was met with rapidly rising subprime origination as lenders searched for new ways to bring additional borrowers into the market. Aggressive changes to loan underwriting guidelines (which peaked in 2006) coupled with new affordability products, allowed many prospective homeowners, who would have ordinarily been shut out of home ownership, to obtain financing. Examples of aggressive underwriting included stated income loans, adjustable mortgages with introductory teaser rates, interest only loans, and loans requiring low or no down payments. As a result of aggressive underwriting, many marginal borrowers have found themselves in homes that they cannot afford. This, combined with the 2007 subprime originator shakeout, resulted in tighter lending standards and set the stage for the performance problems now affecting the subprime market.

Exhibit 1
Historical Serious Delinquencies for Subprime Issuance Years



Serious Delinquencies are loans that are 2 or more payments past due.
Source: Countrywide

Performance

Many of the recent subprime headlines relate primarily to the poor performance of the 2006 vintage. Exhibit 1 shows delinquency rates for subprime vintages from 2001 to 2006 and illustrates how 2006 vintage delinquencies are rising more rapidly than prior vintages. This weaker performance is mostly attributable to lax underwriting compounded by the weak housing market. Based on data from the National Association of Realtors (NAR), the year-over-year decline of -4.7% in home prices (January 2006 to January 2007) is the largest since the NAR began tracking data in the late 1960s. Negative home price appreciation (HPA) combined with tighter lending standards have left many borrowers

with few options if they experience financial hardship. To complicate matters further, 2006 subprime originations were primarily adjustable rate loans with low introductory teaser rates. Historically, when the teaser period expired, borrowers were generally able to refinance easily into new loans at attractive rates. However, the current lending environment has driven subprime rates to their highest level since 2001, making new loans much less affordable.

Structure

With delinquencies rising to higher levels than historically seen, default and loss rates on the underlying subprime loans are expected to be higher for the 2006 subprime vintage than for earlier origination years. Given continued weak HPA and the rapid escalation of 2006 vintage delinquencies, rating agency and investor expectations for cumulative losses on 2006 originated subprime loans have risen to a range of 8% to 12%. Historical loss estimates have ranged from 3% to 5%. The ultimate impact of these higher loss estimates on bonds backed by subprime mortgages are likely to vary widely based on the amount of credit enhancement available to each particular bond within the subprime securitization. Exhibit 2 shows the typical subprime deal structure for 2006 originated deals.

Exhibit 2
Typical Subprime Deal Structure in 2006

Losses

Rating Class and Bond Thickness	Enhancement from Subordination	Cumulative Losses on Pool Required to take Principal Impairment	Cumulative Defaults at the point of Principal Impairment
AAA = 78%	22%	30%	78%
AA = 8%	14%	21%	53%
A+ = 4%	10%	17%	43%
A = 1%	9%	15%	38%
A- = 2%	7%	13%	33%
BBB+ = 1%	6%	12%	30%
BBB = 1%	5%	11%	28%
BBB- = 1%	4%	10%	25%
BB+ = 1%	3%	9%	23%
BB = 1%	2%	8%	20%
Overcollateralization = 2%			
Excess Interest			

Source: JP Morgan and Western Asset

AAA bonds issued off 2006 collateral were generally sized to withstand close to 30% cumulative underlying loan losses, with the remaining rated classes having declining loss coverage depending on each bond's relative seniority in the capital structure. AAA bonds are generally issued as a pass-through (one tranche with a two to three-year average life) or time tranched sequentially, with bonds of varying tenors from an average life of one year to a last cash flow bond (LCF) with an average life of around 8 years. The LCF bonds are generally viewed as the riskiest of the AAA securities, as they are outstanding longer and more susceptible to deterioration of the pool over time. Even with expected losses ranging from 8% to 12%, these LCF AAA bonds are still well protected, holding up to around three times current loss estimates. ***Western Asset has purchased primarily shorter tenor bonds with one to three year average lives, generally avoiding LCF AAAs for the 2006 vintage.***

BBB bonds issued off 2006 collateral were structured so that they could generally withstand approximately 11% cumulative credit losses on the underlying subprime

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collateral. Based on historical cumulative loss expectations of 3% to 5%, BBB subprime bonds could generally withstand approximately two times loss expectations. However, with loss expectations on the rise, many 2006 BBB rated subprime bonds are now at the cusp where at the low end of the new loss expectation range they experience no loss of principal while at the upper end of the range they can lose 100% of their principal. Figure 2 highlights this, as the BBB tranche of any given subprime deal tends to be very thin. Thus, small changes in collateral loss expectations can have a large impact on loss expectations for a particular bond. The figure also highlights that most BB rated bonds from the 2006 vintage would experience losses at levels that are even below current market expectations.

Clearly, these BBB and BB rated bonds no longer have a risk profile consistent with their original ratings. The new loss coverage numbers based on revised loss expectations are more indicative of B to CCC ratings. Thus, it is not surprising that the rating agencies recently announced significant ratings watch lists and downgrades of 2006 vintage BBB and BB bonds (these actions are detailed later in this article). This is likely only the beginning of downgrades as many of these BBB and lower rated bonds could end up defaulting. It is important keep in perspective that the credit issues highlighted by the media concerning subprime will likely be contained to these lower rated bonds. Highly rated bonds from the 2006 vintage, especially AAA rated bonds, are still very well protected from risk of principal loss. Additionally, older vintages of subprime loans are performing much better than the 2006 vintage and should be less susceptible to ratings action given the more conservative underwriting and built in HPA for these loans.

ABX

Recently, ABX, the widely quoted subprime mortgage credit derivative contract, has received a great deal of attention in the press, almost all of it negative. Introduced in January 2006, ABX gave investors standardized derivatives to trade subprime mortgage credit both from the long and short sides. Given its liquidity relative to individual cash bonds, ABX has quickly become a bellwether for subprime mortgage credit. Since ABX contracts are based on an index, investors can make bets on the subprime mortgage market without necessarily having to understand the differences between the underlying deals and originators. ABX has also been a popular way for macro hedge funds to short the housing market.

It is important to note that while the market's reference to ABX is usually the contract backed by BBB- rated subprime bonds, there are actually five separate ABX index contracts; one for each bond rating, AAA, AA, A, BBB, and BBB-. Each index contract contains 20 similarly rated bonds selected to be a representative sample of the subprime mortgage market. The AAA tranche of each ABX series references the LCF bond off each underlying transaction, rather than the pass-through giving it a higher risk profile than the rest of the AAA universe. A new series of ABX is introduced every six months; the constituents of the index will be a representative sample of bonds issued in the preceding six months. To date, three separate series have been issued: ABX 06-1, 06-2, and 07-1.

When the media speaks of the subprime market falling multiple points and widening hundreds of basis points, it is usually referring to the BBB- tranche of ABX. As explained above, this tranche references only the bottom slice of credit risk, rather than the whole subprime bond market. In fact, bonds rated BBB- make up less than 1.5% of the entire subprime market. Broad changes to market loss